

Sale of advertising. Income derived by an exempt organization from the sale of advertising in its annual yearbook is unrelated business taxable income where an independent commercial firm under a contract covering a full calendar year conducts an intensive advertising solicitation campaign in the organization's name and is paid a percentage of the gross advertising receipts for selling the advertising, collecting from advertisers, and printing the yearbook.

Advice has been requested whether, under the circumstances described below, income derived from the sale of advertising by an organization subject to the provisions of section 511 of the Internal Revenue Code of 1954 constitutes unrelated business taxable income within the meaning of section 512 of the Code.

The organization, which has several hundred members and comes within the scope of section 501(c)(5) of the Code, has long followed the practice of having an annual publication, identified as its yearbook, prepared and distributed to its entire membership. This activity entails the assembly for each issue of directory data and other editorial matters of common interest to the distributees, together with the sale of advertising and the related performance of all the usual printing, collection, and distribution services commonly associated with the profitable operation of such a project.

The organization's regular office staff, which includes a full-time director, normally prepares all the editorial materials used in each yearbook or otherwise obtains them on a cost-free basis from governmental or academic sources. Distribution of the yearbook does not tie in with any other organizational activity and is likewise carried out as a regular staff duty from year to year.

Distinctly different arrangements obtain, however, with respect to the solicitation of advertising sales, the printing operation as such, and the subsequent collection of the advertising charges. Contractual arrangements are regularly made with an independent commercial firm for performance of all these operations on behalf of the organization. The current contract covers a full calendar year and also conditionally provides for a continuous series of automatic year-to-year renewals. The commercial firm is paid a fixed percentage share of the gross advertising receipts as compensation for printing the year-book and taking care of all the selling of advertising lineage, printing, and collection functions. Pursuant to this contract, regular annual campaigns of advertising solicitation are carried on in the exempt organization's name from year to year. The intensive phase of each of these campaigns ordinarily continues for only about three months of each year, but no part of the advertising program for which the independent firm has assumed

responsibility varies from customary commercial practice in any material respect.

The term 'unrelated business taxable income' is defined in section 512 of the Code, with certain exceptions and limitations, as the gross income derived by an organization from an unrelated trade or business regularly carried on by it, less allowable deductions directly connected with conducting such trade or business.

Section 513 of the Code defines the term 'unrelated trade or business,' as any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its charitable, educational, or other purpose or function forming the basis for its exemption under section 501.

Section 1.513-1(c)(1) of the Income Tax Regulations provides that specific business activities of an exempt organization will ordinarily be deemed to be 'regularly carried on' if they manifest a frequency and continuity, and are pursued in a manner generally similar to comparable commercial activities of nonexempt organizations. Section 1.513-1(c)(2)(ii) of the regulations provides that, in general, exempt organization business activities which are engaged in only discontinuously or periodically will not be considered regularly carried on if they are conducted without the competitive and promotional efforts typical of commercial endeavors.

Although the publication is distributed only on an annual basis, the advertising solicitation requires that a significant span of time be devoted to these activities. By engaging in an extensive campaign of advertising solicitation, the organization is conducting competitive and promotional efforts typical of commercial endeavors. Thus, the activities manifest a frequency and continuity and are pursued in a manner not materially different from similar commercial activities.

Accordingly, income derived by the organization from the sale of advertising in connection with its annual publication is unrelated business taxable income within the meaning of section 512 of the Code.